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INFO RUCNCLS/ALL SOUTH AND CENTRAL ASIA COLLECTIVE
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RUEHBJ/AMEMBASSY BEIJING 2543
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RUEKJCS/SECDEF WASHDC
RUEKJCS/JOINT STAFF WASHDC
RUEHGV/USMISSION GENEVA 0928
RUEHVEN/USMISSION USOSCE 2936
RUCNDT/USMISSION USUN NEW YORK 2321
RUEHNO/USMISSION USNATO BRUSSELS BE
RUEHBS/USEU BRUSSELS
RUEHLMC/MILLENNIUM CHALLENGE CORP
RUMICEA/USCENTCOM INTEL CEN MACDILL AFB FL

C O N F I D E N T I A L SECTION 01 OF 03 BISHKEK 000588

SIPDIS

DEPT FOR SCA/CEN (GEHRENBECK)

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TAGS: [EMIN](#) [ECON](#) [PREL](#) [KG](#)

SUBJECT: KYRGYZ AND CANADIANS REACH IMPASSE OVER KUMTOR
GOLD MINE

REF: A. 07 BISHKEK 316

[1](#)B. 07 BISHKEK 155

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Classified By: Amb. Marie L. Yovanovitch, Reason 1.4 (b) and (d).

[1](#)1. (C) Summary: Canadian companies Cameco and Centerra Gold have apparently reached an impasse with the Kyrgyz government over a new comprehensive framework agreement for the Kumtor gold mine. The parties entered into the agreement in August 2007, but the Kyrgyz parliament delayed ratification of the agreement. In subsequent negotiations, Kyrgyz officials have reportedly pressed for additional Canadian concessions valued up to \$100-150 million. In mid-May, the Kyrgyz Supreme Court, acting in a case brought by the deputy parliament speaker, issued a ruling that suspended certain previous concession and licensing agreements for Kumtor. In late May, the (twice-extended) deadline for ratification passed, and the August agreement expired. On June 2, Centerra announced that it would pursue international arbitration over outstanding financial issues, and secured a June 23 preparatory arbitration meeting in Bishkek. Prime Minister Chudinov seems convinced that the Canadians have not disclosed all the facts relating to the previous agreement and current operations. Although Kumtor is, for now, still mining ore, the prolonged delay in achieving a ratified agreement and continued legal challenges could hinder Kumtor's operations and further cloud the Kyrgyz investment climate. End summary.

Live and Let Live -- Until Now

[1](#)2. (C) In August 2007, representatives of the Canadian firm Cameco, on behalf of its subsidiary Centerra and its local gold mining concern, Kumtor Operating Company (KOC), agreed with Kyrgyz authorities to double Kyrgyz government holdings in Centerra to 30% (increasing Kyrgyz government holdings by roughly \$300 million) in exchange for a settlement of all outstanding financial questions, an expanded concession and a

comprehensive regulatory and simplified taxation regime. The government decided that the new agreement needed to be ratified by parliament, but early parliamentary elections and the replacement of the prime minister whose team negotiated the 2007 agreement delayed parliamentary consideration of the agreement. As several deadlines passed without ratification, KOC continued to operate under the previous framework agreements, largely without any interruption until this spring. (Note: The Kumtor mine, which has been in commercial production since 1997, represents the largest foreign investment in Kyrgyzstan, and the mine's production is a significant contributor to GDP. End note.)

Bad Cop, Bad Cop

¶3. (C) In mid-April, KOC Vice President of Finance Phil Yee briefed Embassy of a sudden interest by Kyrgyz authorities in KOC's financial records. Spearheaded by the newly empowered Financial Police, Kyrgyz officials, according to Yee, focused on: 1) the coefficient used for land tax assessments already paid (under protest) by KOC; 2) the tax liability for the management fee between KOC and Centerra; 3) a Kyrgyz Chamber of Accounts audit of KOC's files from 1992 to the present; and 4) a tax audit of KOC for 2005-2008. Yee reminded the Financial Police of a moratorium, decreed by Kyrgyz President Bakiyev, of all state tax inspections of businesses. In response, Kyrgyz officials reportedly told Yee that the moratorium "doesn't matter," and that the investigation would continue.

¶4. (C) In late May, Yee reported that teams of Kyrgyz state tax and customs inspectors were reviewing KOC's records as a

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means to "ramp up the pressure" amidst continued renegotiation of the 2007 agreement. The main stumbling block in the renewed negotiations, KOC President Gordon Reid told Emboff June 4, had been a Kyrgyz demand for an additional 10 million Centerra shares with an estimated value of \$100-150 million.

Using Different Playbooks?

¶5. (C) Following an impromptu May 13 tour of the Kumtor mining operation, Kyrgyz Prime Minister Chudinov publicly proclaimed the need to resolve the prolonged negotiations with Centerra. However, the Kyrgyz Supreme Court issued a ruling May 12, in response to a lawsuit initiated by Parliament Vice Speaker Isabekov, which undermined existing agreements and suspended KOC's exploratory activities. (Note: Isabekov, who toured Centerra's Nevada operations earlier this year as part of a Kyrgyz interdepartmental working group, claimed to have gathered revealing documents that presumably supported his opposition to KOC activities. Isabekov has not yet publicly disclosed these documents. End note.) Yee told Embassy that neither KOC nor the Kyrgyz government had been party to any Supreme Court hearing. Reid told Emboff that the ruling had significant "public relations value, but had minimal impact on mining operations." PM Chudinov reportedly directed his administration to challenge the Supreme Court action.

¶6. (C) Chudinov's apparent desire to undo the Supreme Court ruling contrasts sharply with his critical view of Cameco, Centerra and KOC. In a June 5 meeting with the Ambassador, Chudinov implied that the Kyrgyz government had been cheated out of valuable holdings in an earlier renegotiation of the Kumtor mine agreement. He added that KOC's exploration activities, which were curtailed under the Supreme Court ruling, had yielded significant gold for which the Canadians had not paid the Kyrgyz. Yee, in a subsequent June 5 conversation with the Ambassador, countered Chudinov's points by: 1) recounting how the then-Kyrgyz administration approved the renegotiated agreement in which the Kyrgyz side sold a

significant portion of its shares in Centerra; and 2) noting that the minimal amount of gold extracted from one of the exploratory sites had been processed and taxed in accordance with existing protocols.

Impact of Arbitration

17. (C) According to Reid, Kyrgyz requests had prompted Cameco to extend the deadline for Kyrgyz parliamentary ratification of the 2007 agreement. However, Cameco received no similar request before the passing of the latest deadline in late May. Cameco subsequently decided to pursue its arbitration rights to resolve outstanding tax and financial issues that the agreement would have addressed. A Belgian court notified the Kyrgyz ambassador in Brussels June 3 of an arbitration hearing scheduled for June 23 in Bishkek. KOC forwarded a copy of the notification to PM Chudinov's office June 4. Reid expressed his personal hope that arbitration could be avoided, and final agreement could be reached and ratified before the June 23 date.

Investment Climate Implications

18. (C) Although KOC continues to extract gold-bearing ore from the Kumtor mine, the larger business community and potential investors view the prolonged delay in achieving final agreement as a negative indicator of the Kyrgyz business and investment climate. Chudinov recognized this point in his June 5 conversation with the Ambassador. A

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multinational mining firm which met with the Embassy in early April indicated that it is inclined to invest significantly in the Kyrgyz Republic, but in late May notified Embassy that it would wait until the KOC issue is resolved before making a final decision.

Comment

19. (C) Kyrgyz authorities may feel content using audits, lawsuits and other measures to maximize their position vis-a-vis Cameco, but may not be prepared for the intervention of an impartial arbiter. Although arbitration would only address a subset of issues addressed in the mooted agreement, it may persuade the Kyrgyz political elite to take action to obtain agreement and parliamentary ratification. Otherwise, the Canadians and the Kyrgyz could face a lose-lose situation. Any interruption of KOC's core mining activities would have an immediate negative impact on Kyrgyz GDP, depress the value (to include existing Kyrgyz government shareholdings) of Centerra (and likely Cameco) stock and symbolize a significant blow to the Kyrgyz investment climate. YOVANOVITCH